



## Memorandum

JAN 15 1993

Date

From

Bryan B. Mitchell *Bryan Mitchell*  
Principal Deputy Inspector General

Subject

Review of General and Administrative Costs Included in the  
Fiscal Year 1991 Medicare Cost Report by the Medical College  
of Pennsylvania, Philadelphia, Pennsylvania (A-03-92-00015)

To

William Toby, Jr.  
Acting Administrator  
Health Care Financing Administration

This memorandum alerts you to the issuance on January 19, 1993, of our final audit report. A copy is attached.

The report presents the results of our review of general and administrative (G&A) and fringe benefit (FB) costs included in the Fiscal Year (FY) 1991 Medicare cost report submitted by the Medical College of Pennsylvania (MCP), Philadelphia, Pennsylvania. The MCP was 1 of 20 hospitals included in a nationwide review by the Office of Inspector General. This review was in response to a request of the Subcommittee on Oversight and Investigations of the Committee on Energy and Commerce, U.S. House of Representatives.

The primary objective of our review was to determine if the G&A and FB costs reported by MCP on its FY 1991 Medicare cost report were allowable, reasonable, and allocable in accordance with Medicare cost principles. We also determined the relationship of these costs to patient care activities, and whether the costs might be perceived as extravagant or otherwise inappropriate.

The MCP reported G&A and FB costs totaling \$29.4 million, as subject to allocation to Medicare for the year ended June 30, 1991 (FY 1991). Our review disclosed that this amount included \$207,933 which were not allowable for allocation to Medicare. The unallowable costs included \$166,475 for developmental activities, \$26,997 for special events, and \$14,461 for alumnae relations. In our opinion, these costs were not related to patient care.

Under the prospective payment system hospitals are reimbursed prospectively on a per discharge basis. As a result, the inclusion of the \$207,933 of unallowable costs in the FY 1991 cost report resulted in increased Medicare reimbursement of \$3,326. We are recommending that MCP remove these costs from

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its FY 1991 cost report and implement controls to prevent the inclusion of these costs in the future.

Our review also disclosed \$66,729 of costs which we have identified as costs for concern. While these costs were not specifically unallowable under Federal guidelines, there is some concern on the appropriateness of the costs. Recent congressional hearings on colleges and universities have raised questions as to whether these types of costs should be allocated to Federal programs. These costs pertain to various social and employee related activities.

The MCP agreed that many of the costs related to special events and developmental projects were not related to patient care. They believe, however, that these costs were excluded from allocation to the Medicare program through the MCP's allocation methodology. The Health Care Financing Administration regional office stated that the costs identified in this report will be further reviewed by the fiscal intermediary.

For further information contact:

G. A. Rafalko  
Regional Inspector General for  
Audit Services, Region III  
(215) 596-6744

Attachment

Department of Health and Human Services

**OFFICE OF  
INSPECTOR GENERAL**

**REVIEW OF GENERAL AND  
ADMINISTRATIVE COSTS INCLUDED IN  
THE FISCAL YEAR 1991 MEDICARE COST  
REPORT BY THE  
MEDICAL COLLEGE OF PENNSYLVANIA**

**PHILADELPHIA, PENNSYLVANIA**



JANUARY 1993      A-03-92-00015



**DEPARTMENT OF HEALTH & HUMAN SERVICES**

REGION III  
3535 MARKET STREET  
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PHILADELPHIA,  
PENNSYLVANIA 19101

Our Reference: Common Identification Number A-03-92-00015

Mr. Charles Morrison  
Vice President of Finance  
Medical College of Pennsylvania  
One Bala Plaza Suite 434  
Bala Cynwyd, Pennsylvania 19004

Dear Mr. Morrison:

This audit report presents the results of our REVIEW OF GENERAL AND ADMINISTRATIVE AND EMPLOYEE FRINGE BENEFIT COSTS INCLUDED IN THE FISCAL YEAR 1991 MEDICARE COST REPORT BY THE MEDICAL COLLEGE OF PENNSYLVANIA, PHILADELPHIA, PENNSYLVANIA. The Medical College of Pennsylvania (MCP) was 1 of 20 hospitals included in a nationwide review by the Office of Inspector General (OIG) in response to a request from the Subcommittee on Oversight and Investigations (Subcommittee) of the Committee on Energy and Commerce, U.S. House of Representatives. The Subcommittee is conducting an inquiry into the health care system. The MCP was selected in accordance with our objective to include a geographic representation of hospitals nationwide.

The primary objective of our review was to determine if the general and administrative (G&A) and fringe benefit (FB) costs included in MCP's Fiscal Year (FY) 1991 Medicare cost report and allocated to the Medicare program; were allowable, reasonable, and allocable in accordance with Medicare cost principles as set forth in the Provider Reimbursement Manual (PRM); and related to patient care. We also identified costs which, although upheld in the past by fiscal intermediaries (FI) or the Provider Reimbursement Review Board (PRRB), may be perceived to be extravagant or otherwise inappropriate.

The MCP operates four divisions, including a hospital. Costs solely attributed to the hospital as well as costs common to the other divisions are included in the Medicare cost report. Adjustments are then made to eliminate the other divisions' share of the common costs. Following this methodology, the hospital was allocated G&A and FB costs totaling \$12,260,026 and \$17,173,211, respectively. These costs were then allocated to the Medicare program.

We selectively reviewed \$875,166 of the G&A and FB costs allocated to the hospital, and determined that \$207,933 of these costs were unallowable for allocation to the Medicare program. The unallowable costs were included in three common cost centers --Development, Alumnae Relations, and Special Events--and represented that portion of the common costs charged to the hospital after MCP made its adjustments to eliminate the other divisions' share. We believe these costs were unallowable because they were not related to patient care.

**Summary of Review**

Patient care costs	\$144,700,000
Total G&A Costs	12,260,026
Total Fringe Costs	17,173,211
Total Expenses	
Reviewed	\$ 875,166
Unallowable Costs	207,933
Estimated Effect on Medicare Costs	\$3,326

Since the hospital is reimbursed under the prospective payment system (PPS), the unallowable costs that we identified had no direct effect on inpatient reimbursement. These costs directly affected the reimbursement of Medicare outpatient services and excluded units. Accordingly, we are recommending that MCP remove the unallowable costs of \$207,933 from its FY 1991 Medicare cost report, and discontinue allocating these costs to the hospital and thus, to the Medicare program.

In addition to the unallowable costs, we have identified costs of \$66,729 for which we have concerns regarding the nature of the expenditures, and their relationship to patient care. While expenditures of these types have been historically allowed by FIs or the PRRB, we believe they need to be further analyzed in view of increasing health care costs and Federal fiscal constraints. These costs are discussed in the OTHER MATTERS section of this report.

On July 2, 1992, MCP responded to a draft of this report. In response to the information provided by MCP in its response, we have revised or eliminated certain findings that were included in the draft report. As a result, the amount of questioned costs referred to in MCP's response may not be reflected in this final report. We have summarized MCP's response after the Conclusions and Recommendations section of this report, and have included the entire response as an appendix.

## **BACKGROUND**

The MCP, located in Philadelphia, Pennsylvania, is a nonprofit corporation which is a controlled affiliate of the Allegheny

Health Services (AHS), also a nonprofit corporation. The AHS includes the 417-bed MCP, and 5 other hospitals in Pennsylvania.

The MCP operates four separate divisions: an acute care hospital (referred to as the hospital); a post graduate medical school; a faculty practice plan; and a research division. Costs are charged directly to the various divisions based on their relationship to each division. Costs attributed solely to the hospital are included on the hospital and Health Care Cost Report (HCFA-2552), the Medicare cost report, as are common costs that are shared by the hospital and other MCP divisions. The MCP then makes adjustments to the Medicare cost report to eliminate the other divisions' share of the common cost, and to reflect only the hospital's share. The common cost centers and the methodology used to adjust the costs on the Medicare cost report are as follows.

MCP's ADJUSTMENTS TO HOSPITAL COSTS	
COMMON COST CENTERS	PERCENT OF COSTS EXCLUDED
Development	75%
Alumnae Relations	75%
Special Events	75%
Marketing and Public Relations	40%
Professional Fee Billing	100%
Other Shared Services Department	15%

For the year ended June 30, 1991 (FY 1991), MCP reported total hospital operating costs of \$144.7 million before reclassification and adjustments. The net amount subject to allocation to Federal programs was \$138.3 million. Included in the hospital's operating costs were G&A and FB costs originally totaling \$34,089,975. These costs were reduced to \$29,433,237 (\$12,260,026 G&A and \$17,173,211 FB) through adjustments and reclassification of \$4,656,738.

### **Medicare Reimbursement Under PPS**

As previously stated, MCP is reimbursed under the PPS, which was established by the Social Security Amendments of 1983. The PPS is the most common method of reimbursement under Medicare. Today, there are about 6,520 hospitals participating in the Medicare program. About 5,480 of these hospitals, or 84 percent, are reimbursed for inpatient care under PPS. In FY 1991, over \$38 million or 27 percent of MCP's hospital costs were reimbursed by the Medicare program.

Under PPS, Medicare's payment for Part A hospital inpatient operating costs is made prospectively on a per-discharge basis. The discharges are classified into diagnosis related groups (DRG). Hospitals under the PPS reimbursement methodology are reimbursed for inpatient services through fixed DRG payments that are based on the volume and type of service performed, regardless of actual costs. In short, these payments are analogous to "at risk, fixed price contracts" that permit hospitals to make more or less money in treating Medicare patients, depending on how they manage in the aggregate.

Since PPS hospitals receive the same payment for a particular DRG regardless of its costs, inappropriate G&A and FB costs have no immediate direct effect on Medicare reimbursement to these hospitals for inpatient services provided to Medicare beneficiaries. Such inappropriate expenditures, however, do directly effect Medicare reimbursement for outpatient services and for services provided by excluded units. Excluded units are psychiatric, rehabilitation, and alcohol/drug units of general hospitals. According to the FI, Medicare's direct allocation of costs at MCP is 1.6 percent.

## **SCOPE OF AUDIT**

Our review was made in accordance with generally accepted government auditing standards to the extent that they were applicable to the scope of our review as defined in an audit guide developed to ensure adequate audit coverage of the concerns expressed by the Subcommittee. The audit guide was limited to these concerns and, as such, a review of internal controls was not performed.

The objective of our review was to determine if the G&A and FB costs totaling \$29,433,237, which were included in the FY 1991 Medicare cost report and allocated to the hospital were (1) allowable reasonable, and allocable under Medicare cost principles, (2) related to patient care activities, and (3) of a type which may be perceived to be extravagant or otherwise inappropriate.

To accomplish our objective, we selected for review transactions totaling \$875,166 which were included in the G&A and FB accounts in MCP's FY 1991 Medicare cost report, and which were allocated to the hospital. In selecting these transactions, we included only those items which we believed had the greater risk of noncompliance with Federal regulations. Therefore, the results of our analysis cannot be considered to be representative of the overall operations of MCP.

In reviewing the allowability and allocability of costs, we considered whether the costs incurred were (1) reasonable, (2) related to patient care, (3) necessary to the overall operation of the hospital, and (4) deemed to be assignable to patient care in view of the principles provided in the PRM and PRRB rulings. In reviewing the reasonableness of costs, we considered whether or not the individuals that caused the costs to be incurred acted with due prudence in the circumstances considering their responsibilities to the hospital, its employees, its patients, the Federal Government, and the public at large.

During our review of transactions, we classified costs into three separate categories:

- ***Allowable.*** The expenditure is clearly allowable under Medicare as it benefits the provision of patient care.
- ***Unallowable.*** The expenditure is clearly not related to patient care based on its nature.
- ***Costs for Concern.*** The expenditure, in our opinion, may have questionable benefit to patient care. However, these expenditures, such as Christmas parties and costs related to employee morale, have been historically allowed by the FI or the PRRB (discussed under OTHER MATTERS section).

To understand whether costs are allowable, it is necessary to understand the following factors that affect the allowability of costs:

- ***Reasonableness of cost.*** This factor takes into account whether the cost is of a type generally recognized as necessary for the operation of the hospital in view of the MCP's size, scope of services, and utilization (PRM section 2102.1).
- ***Relationship to patient care.*** This factor is defined as including all necessary and proper costs which are appropriate and helpful in developing and maintaining the operation of patient care facilities and activities (PRM section 2102.2).
- ***Prudent Buyer concept.*** This concept requires that providers act as a prudent and cost-conscious buyer and seek to economize by minimizing costs (PRM section 2103).



The PRM section 2102.3 states that:

*Costs not related to patient care are costs which are not appropriate or necessary and proper in developing and maintaining the operation of patient care facilities and activities. Such costs are not allowable in computing reimbursable costs.*

Included in MCP's FY 1991 cost report were costs totaling \$4,941,983 which were allocated from MCP's parent company. These costs were excluded from this review. We are currently conducting an audit of this allocation at the parent company. The results of that review and the effect on MCP's allocation will be reported separately. These home office costs are detailed in the OTHER MATTERS section of this report.

Our field work was performed at MCP's business offices in Bala Cynwyd, Pennsylvania during February and March 1992.

## FINDINGS AND RECOMMENDATIONS

### Unallowable Costs Allocated to Medicare

Included in the FY 1991 Medicare cost report was \$831,731 in common costs from three common cost centers--Development, Special Events, and Alumnae Relations. Following its allocation methodology for common costs shared by the hospital and other MCP divisions, MCP made an adjustment on the Medicare cost report to eliminate the other divisions' share of the common costs, and allocated \$207,933 of these costs to the hospital as shown below.

ADJUSTMENTS TO MEDICARE COST REPORT			
<u>Cost Center</u>	<u>Total Cost</u>	<u>Adjustment</u>	<u>Hospital Allocation</u>
Development	\$665,901	\$499,426	\$166,475
Special Events	107,987	80,990	26,997
Alumnae Relations	57,843	43,382	14,461
Total	<u>\$831,731</u>	<u>\$623,798</u>	<u>\$207,933</u>

As shown above, MCP eliminated 75 percent of the total costs included in the three cost centers, resulting in the hospital sharing in 25 percent of the total common costs for these centers. The FY 1991 Medicare cost report included \$207,933 that was allocated to the hospital.

We reviewed selected transactions from the three common cost centers. In our opinion, none of the costs reviewed were related to patient care. We, therefore, believe that none of the costs should have been included in the Medicare cost report.

### **Development**

The MCP incurred development projects costs of \$665,901 and allocated \$166,475 of these costs to the hospital on the Medicare cost report. We reviewed transactions totaling \$92,742. In our opinion, none of the costs reviewed related to patient care. The transactions were related primarily to fund raising activities. The costs included such things as a campaign feasibility study (\$2,581), pacesetter mailings (\$1,792), consultant for fund-raising (\$1,000), glass jar with oak lid for homecoming (\$804), annual horse show support (\$300), and printing for phonathon fund-raiser (\$108).

*Section 2136.2 of the PRM, states that the costs of fund raising, including advertising, promotional, or publicity costs incurred for such a purpose, are not allowable.*

### **Special Events**

The MCP incurred \$107,987 related to costs for special events and allocated \$26,997 of these costs to the hospital on the Medicare cost report. We reviewed transactions totaling \$29,871. In our opinion, none of the costs reviewed related to patient care. These costs were primarily for outside catering, refreshments, and luncheons and dinner entertainment. Included were items such as catering and staff costs for a hospital dedication reception (\$5,606), Gimble award ceremony (\$4,500), support for annual Womens Way dinner (\$2,500), sponsorship for the Police Athletic League dinner (\$2,500), trolleys for Founders Day reception (\$660), and wine and beer for dedication (\$440).

*Section 2102.3 of the PRM, states that the costs not related to patient care are costs which are not appropriate or necessary and proper in developing and maintaining the operation of patient care facilities and activities. Such costs are not allowable in computing reimbursable costs.*

### **Alumnae Relations**

The MCP incurred \$57,843 related to alumnae relations and allocated \$14,461 to the hospital on the Medicare cost report.

We reviewed transactions totaling \$12,980. In our opinion, none of the costs reviewed related to patient care. The costs were related to the alumnae activities of the medical school. The costs included such items as walnut plaques (\$3,056), alumnae visits (\$539), entertainment for homecoming (\$500), dinner for alumnae executive board (\$392), reunion meeting lunch (\$223), and flowers for alumnae (\$83).

### **Conclusions and Recommendation**

Our selective review of \$875,166 of G&A and FB costs included in MCP's FY 1991 Medicare cost report, and allocated to the hospital, identified \$207,933 of inappropriate expenditures. In our opinion, these costs were unrelated to the provision of patient care and, therefore, unallowable for allocation to the Medicare program.

As stated previously, our review was selective in that we deliberately chose those costs that on the basis of their titles were most likely to be unrelated to patient care. Therefore, the results of our review cannot be considered to be representative of all G&A and FB costs included in the FY 1991 Medicare cost report. It is also possible, however, that because our review was selective, there may have been other costs included in the FY 1991 Medicare cost report that were not related to patient care but were not selected for inclusion in our review.

We are recommending that MCP remove the \$207,933 in unallowable costs identified by our audit from its FY 1991 Medicare cost report, and discontinue allocating such costs to the Medicare program.

### **MCP Response and OIG Comments**

On July 2, 1992, MCP responded to a draft of this audit report and provided additional support for some of the costs that we had questioned in our draft report. We have revised some findings and eliminated others from this final report. Therefore, the amount of questioned costs in MCP's response is not reflected in this final report.

Below, we have summarized MCP's response to the remaining findings and have provided additional comments.

The MCP agreed that many of the costs associated with special events, developmental projects, etc. were not related to patient care. However, these costs were excluded from allocation to the Medicare program

through MCP's allocation methodology. The remaining costs are associated with community service and education activities.

The MCP allocated 25 percent of the total cost of the three common costs--Development, Special Events, and Alumnae Relations--to the hospital on the Medicare cost report. Our review of transactions, totaling \$135,593, showed that not one transaction was related to patient care. This being the case, we believe that none of the costs in the three cost centers should be allocated to the hospital on the Medicare cost report.

## **OTHER MATTERS**

### **HOME OFFICE COSTS**

We did not audit the costs totaling \$4,941,983 allocated from the parent company to MCP. A summary of these costs are as follows.

Senior Officers	\$1,609,482
Legal	924,875
Finance	503,700
Internal Audit	416,524
Human Resources	204,444
Planning	206,158
Information Services	1,812,877
Management Services	36,952
Other Support	311,796
Subtotal	\$6,026,808
Less: Shared Services	<u>1,084,825</u>
Total MCP Home Office	<u>\$4,941,983</u>

We are conducting an audit of these home office costs at the parent company. The results of that review, and the effect on the allocation of home office costs to MCP, will be reported under separate cover.

### **COSTS FOR CONCERN**

In addition to the \$207,933 of unallowable costs included in the FY 1991 Medicare cost report, we also identified \$66,636 of other costs that we have labeled as costs for concern. In some cases, these costs have been historically allowed by the or FI PRRB, however, we question their true relationship to patient care. In other cases, we believe the costs are unallowable, but that MCP may not have allocated them to the Medicare program.

Because of the allocation method used by MCP, it was not possible to reconcile individual transactions to aggregate cost adjustments. Since these costs were included in cost centers where we had also identified allowable costs (unlike the three cost centers mentioned previously), the unallowable costs that we have identified may not be included in the allowable costs allocated to the hospital.

We are reporting on these costs for concern because the Subcommittee specifically requested that we review these types of costs, regardless of whether or not the costs were charged to the Medicare program.

### **Marketing and Other Promotional Costs**

We identified \$29,108 of G&A costs that were expended on marketing and other promotional costs. These costs, in our opinion, were unnecessary in providing patient care and, therefore, unallowable for reimbursement.

Section 2136 of the PRM states that allowability of advertising costs depends on whether they are appropriate and helpful in developing, maintaining, and furnishing covered services to Medicare beneficiaries. The advertising must be directly or indirectly related to patient care. For example, advertising for staff, for procurement of services, or providing visitor hours information may be allowable. Costs for advertising of a general nature designed to invite physicians or patients to utilize the provider's facilities are not allowable.

The \$29,108 of unallowable marketing and photography costs identified in our review included the costs associated with advertising for a bicycle race, photo services for various events, and a press clipping service. These types of costs do not conform to the criteria established in the PRM and, therefore, are unallowable for reimbursement.

The costs, however, may not have been allocated to Medicare since MCP excluded \$102,978 of the total costs in the Marketing and Public Relations cost center from the hospital's allocation.

### **Other Costs for Concern**

We identified \$37,528 of various type G&A costs whose relationship to patient care is unclear. Many of these costs deal with employee-related activities as shown below:

- \$10,215 for clocks, watches, bowls, etc. for employees and friends of MCP.
- \$7,230 for paperweights given to employees and friends of MCP for Founders Day.
- \$2,588 for flowers and fruit baskets for employees and friends of MCP.
- \$2,813 for other miscellaneous flowers and gifts.
- \$4,697 for sponsorship in a bike race.
- \$2,433 for a trip to Italy to inspect a sculpture.
- \$945 for a golf and tennis outing.
- \$615 for other miscellaneous items.
- \$3,613 for retreats at a local hotel. Items listed on the invoices include food and beverages.
- \$1,581 for an employee holiday party.
- \$798 for coffee services and holiday and secretary's day luncheons.

The MCP responded that these costs were principally related to employee recognition and have been accepted in the past. We believe that there is a need to study these costs more closely to determine their true relationship and value to patient care. Costs that appear to improve employee morale have been historically accepted as stated by MCP, and one can argue that the higher the employee morale, the better the services rendered by the employees. The Subcommittee's concern, which we share, is that these employee morale-boosting activities drive up the cost of health care.

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Final determination as to actions to be taken on all matters reported will be made by the Health and Human Services (HHS) official named below. We request that you respond to the recommendations in this report with 30 days from the date of this letter to the HHS action official named below, presenting and comments or additional information that you believe may have a bearing on his final decision.

In accordance with the principles of the Freedom of Information Act (Public Law 90-23), OIG, Office of Audit Services reports issued to the Department's grantees and contractors are made available, if requested, to members of the press and general public to the extent information contained therein is not subject to exemptions in the Act, which the Department chooses to exercise. (See 45 CFR Part 5.)

To facilitate identification, please refer to the referenced common identification number in all correspondence relating to this report.

Sincerely yours,

  
G. A. Rafalko  
Regional Inspector General  
for Audit Services

Appendix

HHS Official

Health Care Financing Administration  
Associate Regional Administrator  
Division of Medicare  
3535 Market Street  
Philadelphia, Pennsylvania 19104

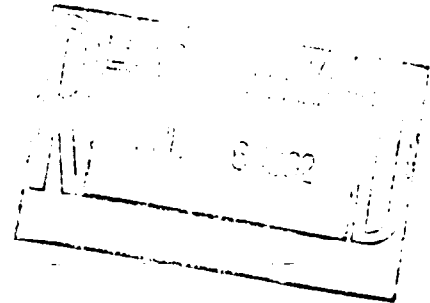
ALLEGHENY  
HEALTH,  
EDUCATION AND  
RESEARCH  
FOUNDATION

Appendix  
Page 1 of 10

100 W. Laurel Avenue  
Cheltenham, PA 19012

July 2, 1992  
VIA: Courier

Mr. G.A. Rafalko  
Regional Inspector General  
for Audit Services  
Department of Health and Human  
Services  
3535 Market Street  
Room 4300  
Philadelphia, PA 19104



RE: #A-03-92-00015

Dear Mr. Rafalko:

We have received a copy of the draft audit report entitled, "Review of Administrative and General Expenses-The Medical College of Pennsylvania for the Fiscal Year ending June 30, 1991." We appreciate the time and effort of your audit staff in conducting their work. It is our objective to fully cooperate with the auditors and to assist them in reviewing the general and administrative (G & A) employee fringe benefit costs at The Medical College of Pennsylvania (MCP). Based upon our review of the draft audit report, it appears that further clarification is necessary to assist in finalization of this report. The purpose of this letter is to submit such clarification to you.

General Overview of Report

The draft report addresses MCP's G & A and fringe benefit costs from the standpoint of allowability and relationship to patient care. It identifies costs in the amount of \$578,341 which were not considered allowable for allocation to the Medicare program. We do not dispute that certain costs identified are unallowable for Medicare purposes. However, the costs allocated to the Medicare program exclude these costs. The draft report and proposed adjustments do not consider MCP's organizational structure and its method of allocation of costs to the Medicare program.



Mr. G.A. Rafalko  
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July 2, 1992

### MCP's Organizational Structure

MCP is not solely a hospital and the costs it incurs are not solely related to patient care. MCP includes four business divisions - (1) medical college, (2) hospital, (3) faculty practice plan, and (4) research division. To ensure that MCP operates in a cost-efficient manner, certain support activities, such as the finance, legal, communications and information services departments, provide services to all four divisions instead of establishing unique support departments for each business division. Similarly, the president's office serves all of the business divisions.

### MCP's Cost Report Methodology

In recognition of MCP's four business divisions, MCP has developed, in concert with the Medicare intermediary, a methodology for ensuring that the costs incurred in supporting the college, faculty practice plan and research division are appropriately excluded from the Medicare cost report. The following describes this methodology.

1. Identification of G & A costs - The G & A costs reported in Columns 1-3 of Worksheet A include G & A costs specific to the hospital, such as utilization review and hospital administration, as well as the total costs of the shared support departments, such as Finance and the President's Office.
2. Through A-8 adjustments, costs included in Columns 1-3 which relate to the college, research division and faculty practice plan are excluded to arrive at allowable costs for allocation to the Medicare program as reported in Column 8 of Worksheet A.

The method to determine the amount excluded through A-8 adjustments is as follows:

Amount Excluded	
Fundraising, Development and Special Events	75%
Marketing and Public Relations	40%
Professional Fee Billing	100%
Other Shared Support Departments	15%

Mr. G.A. Rafalko  
Page Three  
July 2, 1992

This method and the percentages utilized are based upon historically established distributions and are consistent with Medicare's cost allocation methodology. It resulted in elimination of \$2.8 million of G & A Costs from costs allocated to the Medicare program.

3. Through the cost report stepdown process, additional G & A costs are allocated to any hospital-related nonallowable cost centers as identified in Worksheet B.

Comments:

It is important to note that the OIG audit approach focused on the costs included in Columns 1-3 of Worksheet A. -Specific costs were identified as nonallowable without regard to the fact that, (a) MCP consists of four business divisions; (b) it is acceptable for MCP to incur these costs in support of its non-hospital divisions, and (c) those costs were excluded from costs allocated to Medicare.

The methodology does not segregate by division, on an invoice-specific basis, the costs incurred. This would be an extremely inefficient and cost-intensive process. The OIG audit adjustments, however, identify costs on an invoice-specific basis. Since the costs excluded from costs allocated to Medicare are derived through the cost allocation method based upon percentages, it is not possible to tie specific invoices to the costs which are excluded through A-8 adjustments. The methodology is designed to effectively accomplish the exclusion of dollars equal to unallowable costs without incurring the excessive cost which would be necessary to identify the costs on an invoice-specific basis.

The audit did not focus on MCP's method of allocation which has been utilized for numerous years. In 1991, MCP implemented a new general ledger system which combines all four business divisions and provides the ability to more clearly see the total costs incurred by MCP in the operation of its four divisions. As a result of this general ledger implementation, MCP has developed a revised method of allocating shared support and overhead costs to each division. This method was completed in April 1992 and used as a basis of a refiled 1991 Medicare cost report in May 1992. Such cost report, and thus this new method, has not yet been audited by the intermediary.

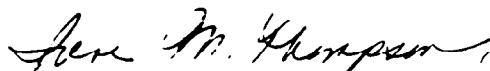
Mr. G.A. Rafalko  
Page Four  
July 2, 1992

Attachment A to this letter addresses key points raised in the draft audit report. I believe this information will clearly point out the concerns we have with the draft audit report.

We believe that MCP has a responsibility to contain costs for the communities we serve. The driving force behind MCP's cost containment guidelines is the fundamental goal to be the lowest-cost provider in our peer group. Further, we are committed to ensuring that costs allocated to Medicare are only those costs that are appropriate and justifiable. Thus, when reimbursement rules are not clear, or when specific expenses may not appear necessary from a payors point of view, we voluntarily exclude these costs. Our recently refiled 1991 Medicare cost report eliminated costs which the OIG auditors questioned, as well as utilized our more sophisticated allocation method.

If I can provide any additional information or clarification, please do not hesitate to contact me. We are committed to fully cooperating with the audit process and commend your staff for the extensive work performed in a very short time frame.

Very truly yours,



Irene M. Thompson  
Regional Executive Vice President and  
Chief Financial Officer -  
Delaware Valley

IMT/lis  
oig

Attachments

Attachment A

Specific Responses to OIG Draft Audit Report Entitled  
Review of Administrative and General Expenses-The Medical College  
of Pennsylvania for the Fiscal Year Ending June 30, 1991

Audit Point:

Based on our review, we found that MCP's controls to prevent unallowable G & A and fringe benefit costs permitted the inclusion of certain unallowable, unreasonable or unallocable costs to the Medicare program in FY 1991.

MCP's Response:

We do not agree with this statement. This statement does not recognize that MCP utilizes an allocation methodology to eliminate costs not related to patient care from the costs allocated to Medicare. At the point in the transaction recording process that the auditors reviewed costs, costs related to all four of MCP's divisions are captured. Subsequent adjustments and allocations eliminate those unrelated to patient care.

Audit Point:

We identified \$307,194 in costs which we believe are unallowable, unreasonable and unallocable. Costs in this group were determined to be clearly not related to patient care based on the nature and type of transaction. These include expenditures related to special events, development projects, alumnae relations, marketing, flowers and gifts, university related expenses and miscellaneous items (e.g. travel, repayments of student loans, sponsorship of activities). These costs should be excluded from the Medicare cost report.

MCP's Response:

We agree that many costs related to special events, development projects, etc. are not related to patient care. We have excluded these costs from the medicare cost report through MCP's allocation methodology.

Audit Point:

The MCP incurred development projects costs of \$665,901 and allocated \$166,475 of these costs to the Medicare program. The MCP incurred \$57,843 related to alumnae relations and allocated \$14,461 to the Medicare program.

MCP's Response:

These costs represent costs of community service and education activities performed by the development staff which has been audited and consistently accepted by the local intermediary. Attachment B summarizes certain of those activities.

Audit Point:

We identified \$29,108 of G & A costs in the FY 1991 Medicare cost report that were expended on marketing and other promotional costs. These costs, in our opinion, were unnecessary in providing patient care and therefore unallowable for reimbursement.

MCP's Response:

The costs of the marketing department include costs for all activities related to media and community relations, public service campaigns, internal communications, volunteer services, marketing and creative services. Many of these activities are related to patient care. Attachment C summarizes the activities of this department.

Audit Point:

We identified \$22,846 of G & A costs in the FY 1991 Medicare cost report that was spent on such things as flowers, clocks, watches, paperweights for Founders Day, etc.

We identified \$8,690 of G & A costs in the FY 1991 Medicare cost report incurred for unallowable miscellaneous items.

MCP's Response:

These costs are principally related to an employee recognition program and the hospital portion of these costs were reported as a fringe benefit cost on the Medicare cost report. The

costs and treatment have consistently been accepted under audit based upon the guidance provided by Provider Reimbursement Manual Part I Section 2144.2. The non-hospital portion of these costs were excluded from the cost report based upon the business division cost allocation process.

Audit Point:

We identified \$271,147 in costs charged to the FY 1991 Medicare cost report for which the documentation supporting the expenditure was not adequate to determine the nature, type, reasonableness or necessity of the expenses. We therefore considered the expenditure to be unallowable and excludable from the Medicare Cost Report.

UNSUPPORTED COSTS

Travel	\$109,327
Credit Cards	36,071
Lodgings	12,425
Miscellaneous	<u>113,324</u>
Total	<u>\$271,147</u>

MCP's Response:

We are reviewing with the audit staff the need for additional documentation and clarification related to these expenditures. We believe we had provided documentation on all but approximately \$50,000 of the documentation requested. Of this \$50,000, \$28,000 relates to the fundraising campaign which was subsequently capitalized and eliminated from expense.

Audit Point:

We identified \$109,327 of G & A costs included in the FY 1991 cost report that were expended for undocumented travel. These costs relate to payments to a travel agency for trips without a stated business purpose.

MCP's Response:

During the field work, invoices from our travel agent were selected by the OIG staff. These invoices include the fares for all travel ticketed by the agent for a month. The MCP accounts payable system posts the total invoice to an

administrative center to facilitate the month end closing process. Subsequently, a staff accountant reviews and reclassifies each fare to the department which incurred the travel cost. As such, \$80,492 of these costs were reclassified to other business divisions which are not included in the cost report. Further, the MCP travel policy establishes the review and approval requirements for costs to be incurred by the institution. While the invoice selected does not list the business purpose of each trip, the departmental and institutional management policies provide controls to assure that all travel costs paid by the institution are for institutional business. We have submitted on a sample basis additional support which typically supports the business purpose of the travel.

Audit Point:

The MCP maintains corporate American Express credit cards for various executives. The charges on this account are routinely processed for payment without justification or identification of business purpose. We identified \$36,071 of such charges included on the FY 1991 Medicare cost report. Our analysis of these costs identified lodging, food (local and out-of-town), ticket upgrades, entertainment, rental cars and other travel costs. We were unable to obtain from MCP supporting documentation showing the nature of these expenses and the relationship to patient care. Therefore, lacking proper documentation, we consider these costs to be unallowable for allocation to the Medicare program.

MCP's Response:

Costs paid by MCP based upon credit card reports are limited to the Senior Management Staff. These costs are subject to the same review and approval policies as other travel and entertainment costs.

Audit Point:

We identified \$12,425 of G & A costs in the FY 1991 Medicare cost report that was spent on lodging costs at a local apartment complex and two local hotels. These facilities were maintained for the convenience of MCP's staff and board members. The MCP was unable to demonstrate the relationship of these facilities to the provision of patient care. Therefore, lacking proper documentation these costs are

unallowable for allocation to the Medicare program and should not be included on the FY 1991 cost report.

MCP's Response:

In an effort to avoid duplication of executive salary costs, certain functions of the AHERF system are managed on a central basis. Due to the geographic location of business units of the AHERF system the staff who are responsible for these functions travel between Pittsburgh and Philadelphia. MCP has leased lodgings in Philadelphia to accommodate these individuals while working locally. We believe the costs incurred for these accommodations are substantially less than the costs which would be incurred to carry the additional personnel and their benefits which would be required to support these management functions. Additionally, our analysis of the costs to lodge these individuals in local hotels indicates that the leases represent a significant cost benefit for providing accommodations.

Audit Point:

We identified additional expenditures totaling \$113,324 for which we requested documentation to support the relationship to patient care. In spite of numerous attempts, we were unable to obtain any supporting documentation from MCP. Therefore, lacking documentation supporting the inclusion of these costs in the Medicare cost report, these costs are unallowable.

MCP's Response:

Our workpapers indicate that supporting documents for all but \$50,000 of the costs selected have been given to the OIG staff either during or subsequent to the field work. At least \$28,000 of the undocumented \$50,000 has been capitalized and is not included in expenses.

Audit Point:

In addition to the \$578,341 of unallowable and undocumented costs included in the FY 1991 cost report, our review also identified \$5,992 of costs for concern.



MCP's Response:

These costs are related to either management functions designed to promote or disseminate new management initiatives and strategies or as morale builders for staff. For example, management retreats offsite are a well-recognized method for allowing management to avoid interruptions when developing or educating a team on new strategies. Similarly, golf outings and holiday parties build morale in many cases for employees who work considerable amounts of overtime but are exempt from overtime compensation. While management agrees that excessive amounts of such costs are inappropriate we believe that, with the proper exercise of judgement, the benefits derived from incurring such costs far exceed the costs which may otherwise be incurred.